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Note by the Secretary-General

The Secretary-General has the honour to transmit to the members of the General Assembly the report of the Joint Inspection Unit entitled "Support costs related to extrabudgetary activities in organizations of the United Nations system" (JIU/REP/2002/3).

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SUPPORT COSTS RELATED TO EXTRABUDGETARY ACTIVITIES IN ORGANIZATIONS OF THE UNITED NATIONS SYSTEM

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JOINT INSPECTION UNIT

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ACRONYMS

ACABQ	Advisory Committee on Administrative and Budgetary Questions
CCAQ	Consultative Committee on Administrative Questions
CEB	United Nations System Chief Executives Board for Coordination (formerly Administrative Committee on Coordination/ACC)
FAO	Food and Agriculture Organization of the United Nations
GEF	Global Environment Facility
ICAO	International Civil Aviation Organization
ILO	International Labour Organization
IMO	International Maritime Organization
IT	Information technology
IWGSC	Inter-governmental Working Group on Support Costs
LDCs	Least developed countries
NGOs	Non-governmental organizations
UNCTAD	United Nations Conference on Trade and Development
UNDP	United Nations Development Programme
UNEP	United Nations Environment Programme
UNESCO	United Nations Educational, Scientific and Cultural Organization
UNFIP	United Nations Fund for International Partnerships
UNFPA	United Nations Population Fund
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organization
UNOPS	United Nations Office for Project Services
WFP	World Food Programme
WHO	World Health Organization

EXECUTIVE SUMMARY: OBJECTIVE, CONCLUSIONS AND RECOMMENDATIONS

OBJECTIVE:
To review the formulation and application of extrabudgetary support-cost policies in the United Nations system organizations, and to propose measures aimed at harmonizing these policies.

A. Formulation of support-cost policies

In the light of frozen or falling core resources, the effective use of extrabudgetary resources in support of mandated programmes has become increasingly important. In reality, however, extrabudgetary activities do not always correspond to legislative priorities, and existing support-cost policies do not reflect, in a systematic manner, the relative importance of particular extrabudgetary activities to these legislative priorities (paras. 4-10, recommendation 9).

Recommendation 1: With a view to ensuring the effective use of extrabudgetary resources in support of mandated programmes, legislative organs may wish to request the executive heads of each organization to:

(a) **Integrate extrabudgetary resources with core resources in budget presentations (as far as they have not already done so) and subject these resources, at least in terms of broad programmatic prioritization, to legislative approval;**

(b) **Accept extrabudgetary resources for activities beyond the reach of core budgets in line with the broad programmatic prioritization approved by legislative organs.**

Most support-cost policies attempt to recover the incremental increase in support costs attributable to extrabudgetary activities. An incremental approach to the determination and recovery of support costs assumes that core functions–fixed costs–should not be financed from extrabudgetary resources. Support-cost policies in most of the United Nations system organizations therefore permit a measure of support to extrabudgetary activities from core resources. The process of defining incremental costs entails an unavoidable element of subjective judgement (paras. 11-14, 17-20, 39).

Recommendation 2: Executive heads should ensure that all incremental cost-measurement exercises clearly define what share of the costs associated with existing administrative and other support structures are appropriately borne by core resources and what must be borne from extrabudgetary resources.

Most support-cost measurement exercises have entailed relatively cumbersome, costly and time-consuming time-work surveys. The management accounting value of a comprehensive survey approach to the measurement of support costs is somewhat overstated. When conducting future cost-measurement exercises, it may be appropriate to focus upon the examination of cost structures prior to conducting a small-scale, and narrowly focused, time-work survey (paras. 26-33, 38).

Recommendation 3: Executive heads should give careful prior consideration to the costs and benefits associated with potential approaches to incremental cost measurement. The validity of the findings of all cost-measurement exercises, including the resulting projections of support-cost income requirements, should be verified using historical expenditure-income analysis.

The practice of UNICEF, and to a certain extent UNESCO, of retaining interest earned on supplementary resources and of using this income to offset support costs, is worthy of further study. This practice can serve to reduce extrabudgetary support-cost rates and eliminate the administrative burden entailed in calculating, crediting, reporting, returning or otherwise determining the distribution of extrabudgetary interest income (paras. 31-38).

Recommendation 4: Legislative organs may wish to consider permitting United Nations system organizations to retain the interest earned on extrabudgetary resources contributed to multi-donor activities where resources are commingled and separate donor-specific accounting is not possible. They may wish to determine that this income should be used to reduce extrabudgetary support costs and that appropriate reporting is made to legislative organs on the relationship between such interest income and support-cost rates.

There are a number of legislative contradictions as regards the extrabudgetary support-cost policies applied by United Nations system organizations. The most common form of contradiction concerns the approval by legislative organs of incremental support-cost recovery policies on the one hand and the approval of legislation proscribing the provision of support to extrabudgetary activities from core resources on the other (para. 47).

Recommendation 5: Executive heads should review the extrabudgetary support-cost legislation applicable to their respective organizations and present proposals to their legislative organs aimed at eliminating contradictions in this legislation.

B. Application of support-cost policies

United Nations system organizations apply a diverse range of extrabudgetary support-cost rates; this reflects the diversity of programme activities, funding arrangements and cost structures. At the level of an individual United Nations system organization, a simple and easily administered support-cost rate is preferable to a complex series of rates but cannot be justified for organizations engaged in a relatively diverse range of substantive and support activities. In these organizations, a relatively straightforward series of clearly defined rates may be more appropriate. A number of United Nations system organizations assess and recover extrabudgetary support costs on a case-by-case basis using a variety of relatively complicated cost-assessment tools. This approach is, however, administratively cumbersome, confusing and inherently inequitable (paras. 40, 43-46).

Increasingly, the validity of a 13 per cent, and in some cases a 10 per cent, support-cost rate is being questioned by donors. Some of these donors have expressed a willingness to finance more transparent and justifiable direct support costs (as direct charges to extrabudgetary resources). Notwithstanding the fact that total support costs, direct and indirect, are ultimately of greater relevance, a number of United Nations system organizations are recovering an increasing proportion of support costs as direct and internal components of extrabudgetary projects and programmes. This approach to the recovery of support costs should not be confused with the new UNDP practice of incorporating the indirect support-cost requirements of United Nations system organizations implementing projects funded by, or through, UNDP as part of the cost of substantive project inputs and expenditures (paras. 20-24 and 41-42).

Recommendation 6: Executive heads of the organizations which have not yet done so, should explore the possibility of including, as direct and internal project or programme costs, identifiable elements presently covered by percentage-based support-cost charges.

Recommendation 7: The Executive Board of UNDP should review the practice of incorporating indirect support costs for United Nations system organizations as part of the cost of substantive UNDP project inputs and expenditures. The Executive Board may wish to revise this policy in line with the principles described in recommendation 9 below.

The authority to grant exceptional support-cost rates is an integral part of most extrabudgetary support-cost policies. This authority is used widely and frequently: it is unavoidable where the resources regarded as extrabudgetary by the recipient United Nations system organization are subject to the support-cost policies of another United Nations system organization (e.g., funds provided through the Global Environment Facility (GEF), the Multilateral Fund for the Implementation of the Montreal Protocol and others); it is particularly prevalent in a number of those organizations required to apply the 13 per cent rate. By definition, exceptions, other than where the support-cost policies of another United Nations system

organization are applied, should be granted infrequently (paras. 47-51).

Recommendation 8: Executive heads should ensure that exceptional support-cost rates, and the grounds on which they are permitted, are consistent. They should only be granted on the basis of justifiable substantive priorities or a genuine determination that lower support-cost rates are appropriate. Furthermore, executive heads granting exceptional support-cost rates on a relatively frequent basis should revise the extrabudgetary support-cost policies to which they are approving exceptions.

C. Harmonization of policy principles

The establishment and application of a single, system-wide support-cost rate, based upon a system-wide cost average that makes no distinction between cost structures, the types of extrabudgetary activity being supported and the nature of this support, would have hardly any present value. A multiplicity of extrabudgetary support-cost rates does not, however, preclude the harmonization of the principles upon which such rates are based. The development of a common approach to the establishment of these rates will significantly improve Member States' understanding and acceptance of support-cost policies of United Nations system organizations (paras. 56-64).

Recommendation 9: Legislative organs should enact support cost policies to ensure that extrabudgetary resources continue to be mobilized and deployed effectively to further the mandated activities in developmental, humanitarian and other substantive areas. These policies should be straightforward, transparent, easy to administer and must provide for a consistent and equitable approach to special arrangements. To this end, legislative organs may wish to consider that:

***(a)* Extrabudgetary support-cost rates should be established in accordance with the following principles;**

They should recognize and reflect the relative centrality, and direct benefits, of an extrabudgetary activity to the mandated programme;

They should be differentiated to take into account the cost of support as influenced by type of activity, conditionality and the volume of resources;

***(b)* The authority to establish extrabudgetary support-cost rates in accordance with the principles in *(a)* above may be delegated to executive heads, with appropriate reporting thereon to legislative organs.**

Recommendation 10: In implementing new extrabudgetary support-cost policies and rates established along the lines indicated in Recommendation 9 above, executive heads should give careful prior consideration to the effect of these changes upon support-cost income, ensuring that a larger proportion of the costs associated with supporting extrabudgetary activities does not fall upon core resources. Any reduction in support-cost income due to reduced support-cost rates should be offset in principle through the achievement of more efficient administrative services.

Recommendation 11: The United Nations System Chief Executives Board for Coordination (CEB) should ensure that the process for establishing support-cost policies be monitored and regular comparative reporting of such policies be developed and disseminated. The outcome of this reporting should be reviewed by appropriate CEB machinery with a view to harmonizing, to the extent possible, the principles underlying support-cost policies, and by executive heads who should report thereon to their respective legislative organs.

Recommendation 12: Legislative organs should continue to monitor overall administrative and other support expenditures and to review these components in the budgets of United Nations system organizations. In so doing, Member States should ensure that administrative and other support requirements in core budgets do not increase in proportion to overall core resources

INTRODUCTION

1. The Joint Inspection Unit (JIU) has examined the issue of extrabudgetary support costs on a number of previous occasions, most recently, albeit indirectly, in its 1990 report on "Extrabudgetary resources of the United Nations".[1] A JIU note in 1978[2] and reports in 1974[3] and 1969[4] focused directly on the cost accounting and cost-measurement aspects of this issue. This report applies a broader, system-wide perspective examining the establishment and application of extrabudgetary support-cost policies. It examines cost-measurement methodologies from a policy perspective rather than a technical perspective. To facilitate preparation of the report, a questionnaire was sent to United Nations system organizations, and the report draws upon the responses to the questionnaire to the extent practicable. The support-cost policies and practices of particular United Nations system organizations (such as the Food and Agriculture Organization of the United Nations (FAO) and the United Nations Children's Fund (UNICEF)), and the support-cost rates of some others shown in the table on page 12, are presented in detail because they are considered to be of general relevance. Examples are also provided where they are deemed illustrative of particular shortcomings or of best practices.

2. This report does not address the use of extrabudgetary support-cost income, the presentation of such income in the accounts and budget submissions of United Nations system organizations, or the extent to which such income is subject to review and approval by legislative organs. In view of the complexity of the extrabudgetary support-cost issue, it has been necessary to assign priority to, and to focus upon, the formulation and application of extrabudgetary support-cost policies. In this context, it should be noted that the questionnaire sought a broader range of responses than can be addressed in a single report; the approach adopted was deemed least likely to result in the omission of essential information.

3. A diverse range of support-cost arrangements and other recovery mechanisms exist in the United Nations system organizations. This complexity reflects the diversity of programme activities, funding arrangements, financial management systems and cost structures. In this regard, a report with a system-wide focus on extrabudgetary support costs must first define the term "extrabudgetary". Extrabudgetary resources are not simply voluntary contributions since the core budgets of a number of United Nations funds and programmes are financed on a voluntary basis. For the purposes of this report, therefore, extrabudgetary resources are "extra", or "supplementary", when compared to those resources that are central to the budget review and approval process of United Nations system organizations. The uses to which extrabudgetary resources are put are not currently reviewed, or approved, in the same detail by legislative organs in the United Nations system. In any study of extrabudgetary support costs, it is also necessary to distinguish between the **costs** incurred supporting activities financed from extrabudgetary resources, the **recovery** of these costs from extrabudgetary resources and the **rates** and other mechanisms by which this recovery is effected. All of these aspects are included in our review of the support-cost policies (for a definition of extrabudgetary support costs, see Chapter II A.).

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[1] JIU/REP/90/3.

[2] "Expanded preliminary notes on a new system for agency support costs" (JIU/NOTE/78/1).

[3] "Report on cost measurement systems in the organizations of the United Nations family and the possibility of developing them into cost-benefit systems integrated into comprehensive management systems" (JIU/REP/74/7).

[4] "Report on the overhead costs of extra-budgetary programmes and on methods of measuring performance and costs" (JIU/REP/69/2).

I. BACKGROUND

A. Extrabudgetary resources

4. The traditional focus of extrabudgetary support-cost studies, and of decisions taken thereon, has been on specific policies and practices pertaining to cost measurement and on the establishment of rates to be applied to the recovery of support costs. While these issues are important and are similarly focused on in this report, it is important to note that they are actually components of a wider political debate on the costs and benefits associated with extrabudgetary resources in United Nations system organizations.

5. The most frequently cited benefits of extrabudgetary financing, as used to justify proposals for lower support-cost rates, are that:

Extrabudgetary financing supports and supplements the core programmes of United Nations system organizations by expanding and strengthening institutional and programmatic capacity, and increasing the delivery of developmental, humanitarian or other substantive benefits;

A greater volume and scope of activities increases the public and political profile of United Nations system organizations, their individual and collective, operational and substantive relevance and their global presence and substantive authority as "centres of excellence".

6. Notwithstanding these benefits, a significant number of Member States are concerned that extrabudgetary activities are:

Being supported, and in effect "subsidized", by core resources and are diverting these scarce resources away from programmes, projects or activities mandated by legislative organs towards those reflecting other priorities of a "narrower" and/or bilateral nature.

Undermining the legislative approval-implementation process and reorienting, or "diverting", the policies, programmes and institutional structures approved by legislative organs away from optimal core resource/ programme configurations.

7. Understandably, these Member States argue that increased contributions to core budgets are preferable to increased extrabudgetary financing. They are supported in this respect by the fact that extrabudgetary resources impose particular planning, management, and reporting requirements upon recipient organizations. Extrabudgetary resources are unpredictable, particularly when compared with assessed contributions. They are generally received piecemeal and are programme, project, or activity specific; they may also require case-by-case review and negotiation, and be tied to certain administrative conditions including specific accounting and reporting arrangements. The administrative conditions attached by donors to extrabudgetary contributions, and the acceptance of these conditions by United Nations system organizations, may incur costs that cannot simply be measured in monetary terms. Examples of these conditions include tied procurement and recruitment, the imposition of specified sub-contractors and an insistence upon special audit arrangements. Notwithstanding these concerns, the significant increase in extrabudgetary resources both in absolute terms, and as a proportion of total resources, is a phenomenon observed across the United Nations system.

8. In response to these concerns, and mindful of the fact that extrabudgetary funding is becoming an ever-larger component of total funding, the Advisory Committee on Administrative and Budgetary Questions (ACABQ), as well as JIU, have made repeated recommendations regarding, inter alia, the need to define precisely the role of extrabudgetary financing in the overall structure of the United Nations system organizations; the need to refine approval and reporting mechanisms so as to ensure that extrabudgetary expenditures are subject to a greater measure of scrutiny and control; the need to identify and explain the role of extrabudgetary funding in relation to activities described in the "core" programme budgets submitted to legislative organs for approval; and, the need to ensure the primacy of United Nations regulations and rules with regard to any conditions attached to special purpose contributions, including through the preparation of

an "Extrabudgetary resources and activities manual".[5]

9. As regards the costs associated with supporting extrabudgetary activities, ACABQ has made repeated recommendations concerning: the need for standard formats and procedures for reporting to donors on extrabudgetary funds with a view to reducing the administrative burden and excessive overheads; the need to ensure adequate reimbursement to core budgets of identifiable expenses related to extrabudgetary activities; the need to develop a mechanism for ensuring that the non-reimbursed use of core budget staff and resources for extrabudgetary activities is minimized to the extent possible; and, the need to ensure that core budget activities do not subsidize extrabudgetary activities and vice versa.[6] The General Assembly has either endorsed or approved these recommendations (see resolution 50/214 of 29 February 1996, for example). Recommendations of this nature are not restricted to the United Nations Secretariat. ACABQ has, for example, expressed concerns that the UNICEF budget does not adequately disclose the costs associated with supporting supplementary activities and has recommended further analysis to enable a determination of which support costs should be borne by general resources and which by supplementary resources or global funds.[7] ACABQ has also recommended that the Executive Board of the United Nations Development Programme (UNDP) review the methodology used to calculate support costs so as to ensure that the administrative and support costs of trust funds are not subsidized by general resources.[8]

10. Most of the point addressed in these recommendations are valid for almost all organizations in the United Nations system and have been raised by Member States at meetings of their legislative organs. They are of particular relevance to this report because fundamental concerns about the cost of supporting activities financed from extrabudgetary resources can only be resolved when Member States, through the appropriate legislative process, are assured that extrabudgetary funding is used in support of programme priorities that have been established by legislative action.

B. The sharing of support costs

11. Whether implicit or explicit, support-cost policies in most United Nations system organizations permit a measure of support to extrabudgetary activities from core resources. Most legislative organs in the United Nations system have approved rates of reimbursement for support costs that are lower than the full costs incurred in supporting extrabudgetary activities and have done so while in possession of cost-measurement studies clearly demonstrating these costs. The founding principle upon which most United Nations support-cost rates are based - the original UNDP formula - considers partial support-cost reimbursement, or the sharing of support costs between United Nations system organizations, and between United Nations system organizations and Member States, as an appropriate financial expression of partnership.

12. In 1975, the UNDP Governing Council approved a rate of support-cost reimbursement of "14 per cent of actual project costs".[9] In decision 80/44 of 27 June 1980, the Governing Council reduced this rate to "13 per cent of annual project expenditures". This level of reimbursement represented, according to cost-measurement studies performed at that time, approximately half of the total support costs incurred (see paragraph 27). The full costs associated with supporting extrabudgetary activities were demonstrated to Member States in a number of detailed studies culminating in, inter alia, reports of the Inter-governmental Working Group on Support Costs (IWGSC) and the Consultative Committee on Administrative Questions (CCAQ) Task Force.[10] In

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[5] "Extrabudgetary Resources of the United Nations" (JIU/REP/90/3). "Advisory Committee on Administrative and Budgetary Questions: 1st Report on the proposed programme budget for the biennium 1990-1991" (A/44/7). "Advisory Committee on Administrative and Budgetary Questions: 1st Report on the proposed programme budget for the biennium 1998-1999" (A/52/7). "Advisory Committee on Administrative and Budgetary Questions: 1st Report on the proposed programme budget for the biennium 2002-2003" (A/56/7).

[6] "Advisory Committee on Administrative and Budgetary Questions: 1st Report on the proposed programme budget for the biennium 1990-1991" (A/44/7). "Advisory Committee on Administrative and Budgetary Questions: 1st Report on the proposed programme budget for the biennium 1996-1997" (A/50/7). "Advisory Committee on Administrative and Budgetary Questions: 1st Report on the proposed programme budget for the biennium 1998-1999" (A/52/7).

[7] "Advisory Committee on Administrative and Budgetary Questions: 1st to 15th Reports on the programme budget for the biennium 1994-1995" (A/49/7).

[8] Ibid.

[9] E/5646.

[10] DP/WGOC/32 and CCAQ/SEC/327 (FB).

its 1974 report on "Cost measurement systems in the organizations of the United Nations family", JIU confirmed the cost measurements taken by the second of these studies as representing "valid orders of magnitude".[11] In its report on the support-cost arrangements embodied in UNDP Governing Council decision 80/44, ACABQ agreed that "the degree of support from the regular budgets of executing agencies to technical co-operation projects financed from voluntary funds is a matter for decision by the legislative organs of those agencies" and recommended that the UNDP formula be approved by the General Assembly for use by the United Nations Secretariat; this recommendation was accepted in resolution 35/217 of 17 December 1980.[12]

13. The 13 per cent rate, and its underlying partnership principle, was subsequently adopted by almost all legislative organs in the United Nations system. A significant number of United Nations system organizations, including the United Nations Secretariat and most of the specialized agencies, continue to apply this rate, albeit inconsistently. Where alternative cost-recovery arrangements have since been adopted, including UNDP's "successor programming arrangements", most continue to be based upon the principle that support costs are to be shared between the recipient organization, the executing organization (if different), and the donor. Recent examples illustrating the continuing relevance of this principle include the following:

Document DP/FPA/2000/2 of 23 November 2000, a report presented to the UNFPA Executive Board, states that "The reimbursement of administrative support costs within and throughout the United Nations system is based on the premise that each agency benefits in some respect from the collaboration of programme funding and execution such that the support-cost arrangement represents a sharing of the total cost of administrative and operational support services."

Documents FC 95/6 and 93/4, presented to the FAO Finance Committee at its 95th session (25-29 September 2000), state that "reimbursement rates have never been set to cover the costs incurred" and traces the origins of this policy to the above-referenced work of UNDP.[13] In the second of these documents, FAO demonstrates a significant rate of under-recovery of support costs and presents this under-recovery as "a legitimate part of the cost of delivering technical assistance to Member Nations". At the 119th session of the FAO Council (20-25 November 2000), it approved a revised policy implementing a system of reduced reimbursement rates.[14]

14. The provision of support to extrabudgetary activities from core resources is not a phenomenon restricted to the United Nations system. Studies by the World Bank indicate that approximately 60 per cent of the average costs of trust fund administration are recovered through fee income. The precise level of the consequent "subsidization" varies and is dependent upon the nature of the extrabudgetary activity and the relationship between the extrabudgetary activity and regular World Bank work. The World Bank applies concessionary support-cost rates when activities financed from extrabudgetary resources require relatively straightforward administrative arrangements or are of central importance to its work.

15. A small number of United Nations system organizations do not apply the partnership principle and are required by their legislative organs to recover the full costs incurred supporting all activities, irrespective of how these activities are financed. In the case of the International Civil Aviation Organization (ICAO), a full cost-recovery policy is applied by the technical cooperation programme, which is entirely financed from extrabudgetary resources, and an incremental cost-recovery policy is applied by the regular programme, which receives a significantly lower volume of extrabudgetary resources. The modalities of full cost recovery are discussed in more detail in paragraphs 21-25 below.

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[11] "Report on cost measurement systems in the organizations of the United Nations family and the possibility of developing them into cost-benefit systems integrated into comprehensive management systems" (JIU/REP/74/7).

[12] A/35/544.

[13] FC 95/6.

[14] CL 119/13.

II. FORMULATION OF SUPPORT-COST POLICIES

A. Defining support costs

16. When examining the costs associated with supporting extrabudgetary activities, it is important to distinguish between direct costs and indirect costs. Essentially, direct costs are those that can be attributed to individual activities while indirect costs are those that cannot. These two basic cost categories can be further divided between fixed and variable costs: costs that do not increase with the volume of activities and costs that do. Applying this categorization, four basic types of support cost are identifiable:

Fixed direct costs: frequently defined as core institutional capacity; these costs include core staff directly responsible for managing, supporting and administering the relevant (often country) programme and its component projects.

Variable direct costs: comprising "internal" project costs including staff, equipment, consultants, travel, communications, premises etc. and "external" project costs such as those incurred during project formulation, presentation, monitoring, evaluation, etc.

Fixed indirect costs: including the costs of an organization's management, central legal services, routine internal and external audit functions, and the operation and maintenance of information technology (IT) infrastructure, financial management systems, central human resources management functions, etc.

Variable indirect costs: including the costs associated with the recruitment and servicing of project staff, consultants and fellowships, procurement actions and contracting, budget preparation and control, project financial operations and accounts and overall extrabudgetary fund raising, reporting, auditing, etc.

17. Most United Nations system organizations apply support-cost policies that attempt to recover variable support costs. This policy, otherwise termed "incremental cost recovery", entails the determination, and recovery, of that increment of an organization's support costs that occurs as a result of an extrabudgetary activity. United Nations Financial Regulation 7.2, for example, states that "voluntary contributions, whether or not in cash, may be accepted by the Secretary-General provided that the purposes for which the contributions are made are consistent with the policies, aims and activities of the Organization, and provided that the acceptance of such contributions which directly or indirectly involve **additional** financial liability for the Organization shall require the consent of the appropriate authority" [emphasis added].

18. An incremental approach to the calculation of support costs assumes that an organization has core functions–"fixed costs"–which should not be financed from extrabudgetary resources as these are unreliable and unpredictable. The difficulties associated with forecasting levels of extrabudgetary funds, and of integrating these resources into core budget review and approval processes, are widely recognized.[15] In light of this fact, support provided to activities financed from extrabudgetary resources by core functions, systems and expertise could be viewed as the recipient organization's key contribution to the partnership described in paragraphs 11-13 above.

19. Of the two categories of variable support costs addressed by incremental cost-recovery policies, internal variable direct costs, as defined in paragraph 16, are almost always financed directly by extrabudgetary resources, as clear and agreed components of the programmes, projects or other activities for which extrabudgetary resources are provided. Since these costs are directly attributable to an extrabudgetary contribution, or group of contributions, and are easily and convincingly justified within the context of the project, programme or activity for which an extrabudgetary contribution is provided, internal variable direct costs are almost always financed in full.

20. The costs usually referred to as "support costs", and therefore the central focus of this report, are the other variable costs: i.e., external variable direct and indirect costs. These costs are far more likely to be questioned by Member States and other donors. The

[15] See ACABQ report A/56/7 for example.

agreement of 9 August 1999 between the United Nations (the Secretariat, funds and programmes) and the European Commission, on the principles applying to the financing or co-financing by the Community of programmes and projects administered by the United Nations, as amended by the 12 October 2000 "second exchange of letters", provides a useful example of the contrast between variable direct and indirect costs and of a donor's perceptions in this regard. This agreement includes a comprehensive list of variable direct costs regarded as "eligible" for funding by the Commission. The list includes: staff, transport, communications and "identifiable personnel costs at headquarters". By way of contrast, the Commission regards the rates applied to the recovery of unidentified variable indirect costs by a number of United Nations system organizations as excessive and will only accept rates of between seven percent and three per cent as a "function of the overall direct cost of the project or programme".

21. As mentioned in paragraph 15 above, a small number of United Nations system organizations are required to recover the full costs associated with supporting all activities. These organizations seek to recover the costs incurred under all four of the categories described in paragraph 16 above. In the case of the World Food Programme (WFP), "each donor is required to meet each contribution's share of all associated costs, including the full operational costs, a pro-rata share of the direct support costs and indirect support costs"; all costs "including management and administration must be funded from each of the contributions made to specific operations".[16] Strictly speaking, United Nations system organizations which are required to recover full costs do not have core resources, "assessed contributions or a core budget with a separate funding mechanism".[17] By corollary, therefore, these organizations do not receive "extrabudgetary resources". In this regard, those United Nations system organizations applying full cost recovery are not the primary focus of this report.

22. Notwithstanding the above, full cost recovery, as practised by WFP and the United Nations Office for Project Services (UNOPS), has resulted in the establishment of percentage-based support-cost rates in these organizations that are lower than in most organizations applying incremental cost-recovery policies. This apparent contradiction must therefore be addressed. In WFP's case, the rate approved by the Executive Board for 2000 is 7.8 per cent; UNOPS does not apply fixed support-cost rates and establishes its recovery arrangements on a case-by-case basis. There are a number of reasons for the comparatively low support-cost rates applied by these organizations. Both WFP and UNOPS, for example, systematically identify and recover as direct and internal project costs, items usually incorporated within the support-cost rates applied by other organizations. Cost components classified by WFP as "direct support costs" can include, for example, country office operating expenses, posts in regional offices, posts at headquarters and other "related costs".[18]

23. In the case of UNOPS, additional indirect costs are often recovered from items presented as direct costs in project budgets. The support-cost rates applied by both of these organizations are also reflective of relatively straightforward operational objectives. WFP also undoubtedly benefits from economies of scale as a result of the nature of its activities while UNOPS benefits from economies attributable to a comparatively lower degree of legislative reporting and oversight, and from simpler and more flexible operating policies and procedures (including those pertaining to geographically equitable recruitment and procurement).[19]

24. As indicated above, a significant reason enabling WFP and UNOPS to apply lower support-cost rates is that they identify, and recover as direct and internal project or programme costs, items the other organizations incorporated within percentage-based support-cost rates. The practice of WFP and UNOPS could be applied to a greater extent than at present by organizations implementing incremental cost-recovery policies. The success of WFP and UNOPS in this regard, combined with the legitimacy accorded to these policies by Member States and other donors, casts doubt upon the continued applicability of an indirect support-cost rate of 13 per cent. All United Nations system organizations could systematically identify and recover a larger

[16] WFP/EB.3/99/INF/18.

[17] Ibid.

[18] WFP/EB.3/2001/5-C/1.

[19] JIU/REP/98/5.

proportion of the support costs attributed to extrabudgetary activities as direct and internal project or programme costs (see paragraphs 20 and 50).

25. Notwithstanding the benefits associated with increasing the proportion of support costs recovered through direct and internal project or programme costs, there are a number of serious disadvantages associated with the comprehensive application of a full cost-recovery approach to extrabudgetary activities. The most significant disadvantages in this regard pertain to the unpredictability of extrabudgetary contributions and the implications of this unpredictability for an organization's financial structure and core programme. As explained in a recent FAO report, full cost recovery "assumes that part of the funding for fixed costs (e.g., the senior management structure) should come from support cost recoveries. However, this could place financial viability of FAO in jeopardy if the extrabudgetary programmes (on which such recoveries rely) were to decline significantly. Income would decline whereas the fixed costs could not–leaving a deficit to be covered by other sources of funds. For this reason, the consultants who have worked on this issue with us and many other United Nations system organizations never recommend the recovery of fixed costs, unless it is unavoidable because an organization relies entirely on support cost recoveries for its income."[20] This report further argued that extrabudgetary donors should not pay for those core staff "who should be funded from the regular programme" because such an approach would result in an element of double budgeting: "if the post of an ADG is to be included in the regular budget and then also charged as an indirect support cost, it is clear that the amount would be appropriated twice". It also argued that "it would be unreasonable to expect a donor to pay for costs which are incurred regardless of whether the project exists or not and which are fully budgeted under the regular programme".[21]

B. Support-cost measurement

26. A number of different approaches have been taken to measuring the costs associated with supporting extrabudgetary activities. The most common approach has been to analyse the extrabudgetary support workload using a time-work survey. This entails the completion by staff of time sheets indicating how much time they spend supporting extrabudgetary activities. These time sheets are then used to define what percentage of overall support costs can be attributed to extrabudgetary activities. This can be done either by costing the time (i.e., by multiplying the time by the standard cost by grade) or by identifying what proportion of total work-hours are spent supporting extrabudgetary activities and then applying this proportion to determine the appropriate and equivalent share of total support-related expenditure. Unless a careful effort is made to omit fixed cost elements and internal variable direct cost elements from a workload survey using time sheets, the full costs associated with supporting extrabudgetary activities, rather than the incremental costs, will be captured. A number of time-work surveys performed by United Nations system organizations have confused the measurement of incremental and full costs, making their relevance to decision-making questionable.

27. The CCAQ Task Force study referred to in paragraph 12 above, covered most organizations in the United Nations system and sought to calculate the full costs associated with supporting extrabudgetary activities. This study arrived at an average support-cost figure of 23.3 per cent. This system-wide average was made up of organization-specific averages, varying from 19.3 per cent for FAO, 31.2 per cent for the United Nations Industrial Development Organization (UNIDO), 22.5 per cent for the United Nations Secretariat, 27.4 per cent for the World Health Organization (WHO) and 29.7 per cent for the International Labour Organisation (ILO).[22] It appears that the once dominant role of UNDP in development financing gave credibility to an exercise of this scope, and to the calculation and use of a system-wide support-cost average. Since the findings of this study eventually led to the adoption of the 13 per cent support-cost rate, however, it is clear that Member States considered its results to be of dubious management accounting value. Given that a full costing approach was used, that participants in this survey must have had a vested interest in securing as large a support-cost percentage as

[20] FC 93/4.

[21] Ibid.

[22] JIU/REP/74/7, op. cit.

possible from UNDP and were subject to relatively lax extrabudgetary oversight, Member States chose to disregard the findings of this survey.

28. The calculation and use of a system-wide average support-cost percentage that makes no distinction between the types of extrabudgetary activity being supported and the nature of this support, would have hardly any present value. At the level of individual United Nations system organizations, a simple and easily administered support-cost rate is preferable to a more refined schedule of rates but can only be justified from a cost-accounting perspective for organizations using extrabudgetary resources for relatively similar programmatic activities requiring relatively similar support functions. A meaningful degree of differentiation in substantive and support activities makes it difficult to justify an average rate on grounds other than ease of administration. Recent organization-specific cost-measurement exercises, such as those conducted by FAO and UNICEF, have sought to achieve more appropriate objectives.

29. The FAO study referred to in paragraph 13 above, followed two distinct stages. The first stage, "using a full costing methodology" required staff graded from D-1 to G-5 (G-4 in some cases) to complete a detailed questionnaire in which they estimated the percentage of their time spent on regular programme activities vis-à-vis extrabudgetary activities. With respect to the latter, they were also asked what percentage of time they spent providing technical support services to projects, administrative and operational services to projects and services to WFP. A time-work survey on this scale was considered by FAO to "far exceed the requirements for statistical reliability". At the end of the first stage, the findings of the time-work survey were calculated to give the full cost figure. This was achieved by means of a two-step calculation: time was multiplied by the standard cost by grade to arrive at the staff cost, and to this amount, allocation was made for the cost of administrative departments using "the most appropriate statistical keys for measuring the workload attributable to those units" (e.g., space utilization, staff numbers, accounting transactions, etc.). In the second stage of this exercise, the full cost figure was reduced through the elimination of "fixed overhead costs" to arrive at "indirect project support costs".

30. These "fixed overhead costs" included:

All costs related to management and policy offices (excluding their immediate support units which were allocated to indirect project support costs using the work measurement questionnaire);

All fixed overhead costs related to the operation and maintenance of IT infrastructure (except for those costs charged directly to departmental budgets which are treated as direct project costs or as indirect project support costs, as applicable);

All costs of the operation of the financial system (except those units directly responsible for extrabudgetary accounting which were treated as indirect project support costs);

All costs of administering the central personnel function; costs of space, security, communications, messenger service, central records and procurement for core programme activities (except as directly charged to projects);

Costs of core budget preparation, control and evaluation (although costs of project budgetary control and evaluation are treated as indirect project support costs or, in the case of evaluation missions, as direct project costs);

Costs of legal services (excluding technical services to projects which are treated as direct project costs);

Costs of internal and external audit (excluding direct services provided to projects).[23]

31. A 1998 UNICEF study applied a simple cost identification-elimination approach to cost measurement using a desk review rather than a wholesale survey, on the grounds that the UNICEF Executive Board preferred this to a more complex and costly accounting system. This approach entailed the examination of cost structures and the subtraction of fixed costs and internal variable direct costs from these structures. By a process of elimination, UNICEF identified the residual indirect variable

[23] FC 93/4, op. cit.

costs associated with supporting the supplementary-funded programme and estimated the support-cost rate that would need to be levied on supplementary resources in order to recover these costs. Since UNICEF is permitted to retain the interest earned on supplementary funds, and to use this income to offset the cost of supporting the supplementary-funded programme, the support-cost rate was calculated to meet the requirement for indirect variable costs minus interest income. The fixed costs which were eliminated using this approach included:

> Substantive support representing the costs of UNICEF's basic programme and advocacy presence in a country; operational support which represents the cost of the operational function required for the proper execution of the mandated responsibilities of UNICEF;
>
> Common general operating costs which include the operating expenses required for maintaining and running UNICEF offices;
>
> Management functions that are maintained regardless of supplementary-funded activities.

The identification of support costs for supplementary-funded programmes at UNICEF headquarters entailed a division-by-division examination of cost structures and the elimination of fixed costs. The cost structure of a single medium-sized office was studied and the support-cost requirement identified following the elimination of all fixed costs was presented as being applicable to all country and regional offices.[24]

32. Both of these approaches to cost measurement were acceptable to Member States in the legislative bodies of FAO and UNICEF and can be regarded as good practice. They are both relatively transparent: cost-measurement objectives and foci are carefully and clearly defined, explained and justified. Since the process of defining cost-measurement parameters entails a significant and unavoidable element of subjective judgement, the importance of transparency as regards this aspect of cost measurement cannot be overstated. In theory, the comprehensive time-work survey approach employed by FAO is more likely to generate statistically reliable and empirically justifiable results. The comprehensive time-work survey approach to cost measurement will also provide useful information as regards the fixed and direct variable costs associated with extrabudgetary activities. It may also provide useful micro-level management information as regards the volume, type and displacement of work generated by extrabudgetary activities. Notwithstanding these advantages, comprehensive time-work surveys are relatively cumbersome, costly and time-consuming. They are over-dependent upon the accurate completion and assessment of detailed questionnaires. A questionnaire completed in November of each year may not, for example, necessarily facilitate the accurate calculation of the average time spent supporting extrabudgetary activities over the course of a budget/financial period.

33. A broader funding issue may also have to be factored into the use of, and the assessment of results from, time-work surveys. In United Nations system organizations experiencing falling or frozen core budgets, larger proportional cuts may have been made in non-staff core budget items than in core budget staff. In these circumstances, core budget fixed costs have risen in proportion to core budget variable costs and some United Nations organizations have acquired a measure of institutional over-capacity. Put more simply, programme managers on core posts have fewer core resources with which to undertake substantive activities. These managers need extrabudgetary resources to function and quite naturally expend significant amounts of time and effort raising and using these resources. In this regard, a time-work survey showing a high proportion of time spent supporting extrabudgetary resources may not reveal the true costs associated with supporting extrabudgetary activities. It may instead reflect a "distorted" core budget structure, a relative scarcity of non-staff core resources and a resulting over-dependence upon extrabudgetary resources. In these United Nations organizations, the use of time-work surveys may be less appropriate to the assessment of extrabudgetary support costs than the UNICEF cost identification-elimination approach.

34. The narrower cost identification-elimination approach used by UNICEF is probably, from a cost accounting perspective, less accurate. The use of a single "medium-sized office" to estimate all country

[24] E/ICEF/1998/AB/L.6.

and regional office support costs is particularly problematic in this regard. The tighter focus of a cost identification-elimination approach will certainly not generate the same range of management information. From a management accounting perspective, however, this approach may be entirely appropriate. An important reason for this pertains to the fact that the Executive Board of UNICEF approves supplementary-funded programmes. This, to a large extent, addresses Member States' concerns regarding the use of core "multilateral" resources to support extrabudgetary "bilateral" activities. Similar measures for other United Nations organizations could considerably reduce the political significance attached to the support-cost issue. The relatively limited importance attached by UNICEF's Executive Board members to the "subsidization" issue is evinced by their endorsement of a study showing that, in 1998-1999, "93 per cent of supplementary funds [were] expected to be distributed directly to programme activities, compared to 59 per cent for general resources" and that for four biennia, 1992-1999, "general resources have absorbed a larger proportion of the increase in programme support costs".[25]

35. At the 119th session of the FAO Council (20-25 November 2000), a revised policy implementing a system of reduced reimbursement rates was approved.[26] These rates vary from 6 per cent for emergency assistance and activities of direct relevance to core programmes, to a maximum of 13 per cent for technical assistance. At its second regular session (8-11 September 1998), the Executive Board of UNICEF accepted that the support-cost requirement for supplementary funding "can be met from the interest income plus a 5 per cent recovery". At that time, interest earned by supplementary resources provided UNICEF with support costs equivalent to an additional rate of recovery of approximately 4 per cent.

36. The retention of interest earned on extrabudgetary resources, particularly those that finance multi-donor activities, could be beneficial to all United Nations system organizations because it can be used to offset support costs and because such funds are commingled: this would eliminate the need to calculate, credit, report on, return or otherwise determine the distribution of extrabudgetary interest income. However, interest earnings are invariably lower than support costs and cannot fully replace the application of a percentage-based charge as a means of cost recovery. The recovery of support costs from interest income, which by its nature is subject to changes beyond the control of United Nations organizations, may require these organizations to make corresponding and relatively frequent adjustments to support-cost rates. Since administrative costs are already subject to changes in market conditions, including inflation and exchange rates, the need to factor an additional externality into cost-recovery considerations would not place an undue administrative burden on United Nations organizations.

37. Potential arguments against the retention of interest income include: the possibility that United Nations organizations will attempt to control extrabudgetary expenditures in order to keep extrabudgetary funds in interest-earning accounts; the existence in donors' domestic legislation of prohibitions on the retention of interest income by United Nations organizations; and, the perception that donors will end up paying more for support costs than is the case at present. The experience of UNICEF, UNESCO and of other United Nations organizations where interest earned by multi-donor accounts is retained on the grounds that it is impractical to return it to individual donors, may suggest that none of these problems are insurmountable. Member States may wish to consider the possibility of extending the policy of retaining extrabudgetary interest income, and of using this income to reduce extrabudgetary support costs, to other United Nations organizations. In the application of this policy, however, Member States should monitor extrabudgetary expenditures closely and United Nations system organizations should maintain, and routinely update, the transparent and proportional relationship between interest income and support-cost rates.

38. It may be useful when conducting future cost-measurement exercises for United Nations system organizations to combine the strengths of the FAO and UNICEF approaches described in paragraphs 29 to 31 above. As the first step in a cost-measurement exercise, it may be more appropriate to examine cost structures with a view to eliminating obvious fixed costs and internal variable direct costs. The

[25] Ibid.

[26] CL 119/13, op. cit.

remaining offices could then be surveyed using a straightforward questionnaire. This two-step approach entails a smaller-scale and more focused time-work survey than that conducted by FAO, and a more reliable, and empirically justifiable, approach to cost estimation than that used by UNICEF. The validity of the findings of all cost-measurement exercises, including the resulting projections of support-cost income requirements, should be verified by historical expenditure-income analysis. This entails tracking proportional changes in core programme and programme support expenditures alongside extrabudgetary support-cost income. By these means, proposed support-cost rates would have to be justified in relation to previously acceptable core programme-to-core programme support ratios and previous levels of extrabudgetary support-cost income. Rates for succeeding periods would have to be adjusted to reflect any under-recovery in the preceding period.

C. Determining support-cost rates

39. As illustrated in paragraphs 29 to 31 above, all attempts to calculate the "external" variable direct costs and the variable indirect costs associated with supporting extrabudgetary activities seek to define what share of the costs associated with existing administrative and other support structures are appropriately borne by core resources and what must be borne from extrabudgetary resources. While a range of technical criteria can be applied to this process, it is clear that a significant element of subjective judgement is exercised. It is also clear from the responses received to the questionnaire that a number of managers in the United Nations system organizations regard support-cost rates as a resource prioritization issue with cost accounting dimensions. In marketing terms, managers often see support-cost rates as the "price" at which they "sell their services" to extrabudgetary donors. Under these circumstances, rates are established by weighing donor positions alongside their organization's cost absorption capabilities. Cost-measurement exercises then become rate-justification exercises. The only way to address this issue is to eliminate the negative connotations attached to the support of extrabudgetary resources from core resources by ensuring that extrabudgetary resources are applied to appropriate purposes (see recommendation 1).

III. APPLICATION OF SUPPORT-COST POLICIES

A. Support-cost rates

40. Responses to the questionnaire referred to in paragraph 1 revealed that an increasingly diverse range of extrabudgetary support-cost rates are applied in the United Nations system: the rates used by eight United Nations system organizations are shown by way of example in the table below. These organizations were selected to illustrate the multiplicity of support-cost rates applied by United Nations system organizations on the grounds that the diversity of rates and policies applied by these organizations can be regarded as representative of those applied throughout the United Nations system. Given the diverse range of programme activities, funding arrangements and cost structures in the United Nations system, multiple support-cost rates are undoubtedly appropriate. What is appropriate at the system-wide level, however, may not be appropriate at the organization level. For United Nations system organizations engaged in a relatively broad range of substantive and support activities, the merits of activity-specific cost assessment and support-cost rates must be balanced against the costs and other difficulties associated with administering a complex extrabudgetary support-cost recovery system. Transparency also requires a measure of simplicity. In this context, a relatively straightforward series of clearly defined rates may be the most appropriate means of achieving this balance.

Extrabudgetary support-cost rates applied by eight United Nations system organizations

ORG.	SUPPORT-COST RATES	
ICAO	1. Governments:	*Trust funds and private funding:* - 13 per cent for charges approved before 2001 - 10 per cent for charges approved from 2001 *Handling charges for management services agreements* - 6-10 per cent for services implemented at the international level - 3-9 per cent for services implemented at the local level *Civil Aviation Purchasing Service (CAPS)* - 6 per cent for the first US $100,000 - 4 per cent from US$ 100,001 to US$ 500,000 - Negotiable above US$ 500,000 - In addition to the above, ICAO also charges, on a full cost-recovery basis, for technical support services when it has to prepare detailed technical specifications, system designs, etc.
	2. United Nations sources (UNDP, etc.):	- 10 per cent for administrative and operational support (AOS) - 8 per cent or lower for repeat and large procurement items - 3.5 per cent for UNDP Government cash counterpart contribution projects
	3. Other sources:	- 5-7 per cent for the European Commission
ILO	- 13 per cent standard for multi-bilateral funding - 12 per cent standard for associate professional officers - 10 per cent for UNDP	
IMO	- 13 per cent standard - 12 per cent for Associate Professional Officers - 10 per cent for UNDP - Reduced rate for the European Commission and the World Bank	

Table continued on the next page

ORG.	SUPPORT-COST RATES (con't)	
UNCTAD	- 13 per cent standard - 3-7 per cent for the European Commission - 5 per cent for the United Nations Environment Programme (UNEP) and the United Nations Fund for International Partnerships (UNFIP) - 0-10 per cent for UNDP	
UNESCO	1. Governments, private funding, and international financial institutions:	- 13 per cent standard - 12 per cent for the associate experts scheme - 8 per cent for projects consisting exclusively or very largely of the procurement of equipments - 5 per cent for projects requiring very little supervision - Rates on a case-by-case basis for projects executed to the benefit of LDCs
	2. UNDP sources:	- Up to 10 per cent for administrative and operational support
	3. UNFPA sources:	- 7.5 per cent of the project direct costs, except for international and global projects
	4. European Commission:	- Rates are negotiated for every agreement to reflect the backstopping needs of each project
UNFPA	- 5 per cent for managerial support services - Up to 12 per cent for administrative and operational support depending on the executing agency - 3-7 per cent for the European Commission - 5 per cent for UNFIP	
UNIDO	- 13 per cent for non-UNDP projects - 10 per cent (plus technical services work months) UNDP, the Global Environment Facility (GEF) and chlorofluorocarbon (CFC) projects - 13 per cent for Montreal Protocol for the first $500,000; 11 per cent for any delivery per project above that amount - For some individual projects, other rates are granted by the Director General upon the advice of the Director, Financial Services (mainly GEF-funded projects)	
WHO	- 13 per cent standard - 12 per cent associate professional officers - 6 per cent supply services/emergencies (except preparedness) for countries covered by United Nations consolidated appeal and for certain bulk procurement - 5 per cent on contributions from certain donors including Rotary International for Polio and UNFIP - 3 per cent for non-emergency supply services to Member States, NGOs in an official relationship with WHO or members of the United Nations family - 0 per cent for emergency supply services to Member States, NGOs in an official relationship with WHO or members of the United Nations family, and for purchases made through the revolving fund for teaching and laboratory equipment for medical education and training	

41. The issue of transparency is particularly relevant in light of recent changes made by UNDP to the management of the indirect support-cost requirements of United Nations system organizations implementing projects funded by, or through, UNDP. Since 1992, UNDP has reported and reimbursed these support costs, up to a maximum of 10 per cent of the cost of substantive project inputs, as a separate and distinct cost element in project budgets, termed Administrative and Operational Services (AOS). A main objective of the 1992 AOS arrangement was to make support costs more transparent. In a 25 March 2002 communication to all "UN Executing/ Implementing Agencies", however, UNDP stated that, effective 1 January 2002, "AOS would no longer be reflected as a separate cost element in UNDP project budgets or in the related expenditure reporting." Instead, "AOS is

now included as part of the cost of the pertinent inputs at the budget (sub)line level"; i.e., incorporated as part of the cost of substantive project inputs and expenditures. The principal reason given for this change in policy is that major donors "were not willing to reimburse support costs when presented in the AOS column" because "they tended to view separately recorded support costs as additional UN system overhead charges". The new policy, which effectively hides the full cost of supporting a UNDP project, is expected to "facilitate negotiations with new partners".

42. The lack of transparency involved in the practice described above has significant implications for UNDP. Member States and other donors no longer know what part of a planned contribution to UNDP will be, or was, used for substantive purposes and what part will be, or was, used to reimburse United Nations system organizations' administrative services. By concealing a significant proportion of the costs incurred supporting UNDP projects, Member States and other donors will no longer be able to make informed decisions aimed at maximizing the substantive impact of their contributions. In relation to other, more transparent, United Nations system organizations, UNDP will erroneously appear more cost-efficient and cost-effective.

43. A number of United Nations system organizations, including UNOPS, assess and recover extrabudgetary support costs on a case-by-case basis using a variety of relatively complicated cost-assessment tools. The most frequently cited advantage of an activity-specific and contribution-specific cost-recovery policy is that it will eliminate under- and over-recovery. In reality, however, such an approach is cumbersome, difficult to administer and confusing to donors. A lack of clarity as regards appropriate charges may encourage donors to negotiate lower support-cost rates and may necessitate United Nations system organizations recovering a larger proportion of support costs from some other donors in order to compensate for the under-recovery of costs. The process of negotiating support-cost rates for each and every contribution is inefficient, time-consuming and inherently inequitable; the application of a consistent and transparent policy to the establishment of support-cost rates would eliminate many of these concerns.

44. The administrative burden imposed by an activity-specific costing methodology is demonstrated *in extremis* by UNDP's cost-recovery system for operational services provided to other United Nations system organizations by UNDP country offices (of which there are 132). According to the Guidelines for Operational Support Services by UNDP at the Programme-Country Level (UNDP 1999), the basic instrument for the recovery of support costs associated with the provision of support services to other United Nations system organizations is the service charge. These charges are determined by each country office and are "tailored" to country-offices' cost structures and local conditions. Each country office has the authority to determine what costs to recover and what cost-measurement method to apply. They are also authorized to negotiate and conclude the requisite service-provision cost-reimbursement agreements with individual United Nations system organizations.

45. One UNDP country office has, for example, established a schedule of service charges with 37 components including: US $244.10 for recruitment against a fixed-term contract, US $80.63 for arranging the registration of a vehicle, US $17.67 for the recruitment of a consultant, US $5.20 for the issuance of a consultancy contract, US $5.02 for the issuance of a travel authorization, US $2.89 for making a hotel reservation and US $2.31 for the registration of in-coming correspondence. This particular UNDP office based its schedule of costs upon the findings of a time measurement study and transmitted this schedule, together with a carefully formulated agreement, to all United Nations system organizations that may wish to use their services. These agreements commit this UNDP country office to present quarterly bills for reimbursement indicating all the requests made and services provided. The administrative burden imposed by this system falls upon users as well as operators: an organization like UNESCO, for example, would conceivably have to conclude and manage over 100 individual cost-recovery agreements of this type with UNDP country offices.

46. The approach described above has understandably aroused the concerns of UNDP's partner organizations and is presently under review. It is hoped that the revised system will drastically simplify, and centralize, UNDP's country office cost-recovery arrangements. All rates and other charges used to recover extrabudgetary support costs must be straightforward, transparent and easy to administer.

47. Responses to the questionnaire also revealed a number of legislative and other contradictions as regards the extrabudgetary support-cost policies applied by United Nations organizations. The United Nations Secretariat, for example, is required by General Assembly resolution 35/217 of 17 December 1980, to apply the UNDP-formulated partnership principle embodied in the 13 per cent support-cost rate. Notwithstanding this principle, in a further resolution–50/214 of 29 February 1996– the General Assembly endorsed a recommendation of the ACABQ to the effect that core budget activities are not to subsidize extrabudgetary activities. A similar contradiction exists as regards the application by the ILO of the 13 per cent rate and its financial regulations prohibiting the use of core funds for any purposes not provided for in the approved programme and budget. All United Nations system organizations should revisit their support-cost legislation and present proposals to their legislative organs aimed at eliminating such contradictions.

B. The granting of exceptions

48. A survey of official support-cost rates, and an examination of the policies behind the establishment of these rates, does not reveal the complete picture as regards the recovery of extrabudgetary support costs. The authority given to the secretariats of United Nations system organizations to grant exceptional support-cost rates is an integral part of most extrabudgetary support-cost policies. This authority is used widely and frequently: it is unavoidable where the resources regarded as extrabudgetary by the recipient organization are provided by, or through, another United Nations system organization and are subject to that organization's support-cost policies (e.g., funds provided through the GEF, the Multilateral Fund for the Implementation of the Montreal Protocol and others); it is particularly prevalent in a number of those organizations required to apply the 13 per cent rate. The extent to which exceptional rates are granted can be ascertained by a straightforward examination of United Nations system organizations' accounts, i.e., comparison of total extrabudgetary support-cost income in relation to total extrabudgetary expenditure. In most cases, support-cost recovery falls far short of what would be expected if the support-cost rates approved by legislative organs were consistently applied to all extrabudgetary expenditures. Both the United Nations Secretariat and UNESCO, for example, recover on average approximately 7 per cent of extrabudgetary expenditures as support costs, in spite of the fact that both of these organizations theoretically apply the 13 per cent support-cost rate. Exceptional support-cost rates, other than where the support-cost policies of another United Nations system organization are applied, are granted for a number of reasons, including:

- To maximize the availability of resources for activities that are central to an organization's mandate but were not foreseen at the time of the preparation of core budgets, e.g., the provision of emergency humanitarian relief;

- Lower support-cost requirements attributable to simple and straightforward operational objectives (e.g., procurement) or to the use of alternative cost-recovery modalities (e.g., direct cost recovery);

- Lower support-cost requirements attributable to large scale contributions for activities that, in support terms, benefit from economies of scale;

- Member States' and other donor dissatisfaction with support-cost policies;

- The need to cope with falling or frozen core budgets by improving an organization's ability to compete for extrabudgetary resources.

49. By definition, exceptions should be granted infrequently. Other than where the support-cost policies of another United Nations system organization are applied, exceptional support-cost rates and the grounds on which they are permitted, must be consistent. They should only be granted on the basis of pre-determined substantive priorities

and/or a justifiable determination that lower support-cost rates are appropriate. Member States' and other donors' dissatisfaction with support-cost rates are insufficient grounds on their own on which to allow exceptions. In this context, approximately one third of respondents to the questionnaire admitted that their organization granted exceptional support-cost rates at donor insistence. The agreement between the United Nations Secretariat, the funds and programmes and the European Commission, referred to in paragraph 20, is a significant example of an exception to established support-cost policies made at donor insistence. The importance of donor demand in this area may even be more significant than has been reported.

50. An increasing number of Member States and other donors appear dissatisfied with a 13 per cent, and in some cases a 10 per cent, support-cost rate. Some of these donors regard these rates as being excessive, unjustifiable and an obstacle to the provision of extrabudgetary resources. It is worth noting that an increasing number of Member States in receipt of United Nations-executed extrabudgetary programmes, projects and other activities also object to relatively high support-cost rates, particularly where the resources in question have been loaned or granted by multilateral development banks and other donors. In addition to objections to the effect that the 13 per cent support-cost rate is too high, a number of Member States and other donors have objected to the lack of transparency inherent in a percentage-based charge. Some of these donors have expressed a willingness to finance justifiable direct administrative expenses, presuming, of course, that these can be identified. Where arrangements to this effect have been accepted, United Nations organizations have often identified, and recovered, components of the 13 per cent directly from the principle contribution (see paragraphs 20 and 24).

51. Where the granting of exceptions is commonplace, established extrabudgetary support-cost policies are probably inflexible and need to be reviewed, and in all likelihood revised. In the United Nations Secretariat, for example, a measure of consistency has been applied to the granting of exceptional support-cost rates. Over a number of years, these exceptions have developed into an alternative, more flexible albeit informal, extrabudgetary support-cost policy. The United Nations Secretariat either waives support-cost rates entirely, or levies a rate of up to 3 per cent, on extrabudgetary contributions for humanitarian emergencies. Where the United Nations Secretariat acts as a substantive co-ordinator and a trust fund manager but not as the executing entity, e.g., for funds transferred to other organizations for utilisation, a 3 per cent rate is usually applied. The United Nations Voluntary Trust Fund for Mine Action applies this support-cost rate. Extrabudgetary contributions towards core activities, such as are provided to the trust funds for United Nations missions in Kosovo and East Timor, are effectively "subsidizing" core resources and are charged a support-cost rate of 5 per cent. All other extrabudgetary contributions to the United Nations Secretariat are charged the official 13 per cent rate. Given the diversity of substantive and support activities performed by the United Nations Secretariat, a simple and transparent schedule of support-cost rates is clearly appropriate. The Secretary-General should revise the United Nations Secretariat's official extrabudgetary support-cost policy accordingly.

52. Responses to the questionnaire revealed a number of circumstances where extrabudgetary support-cost policies are waived in their entirety. The routine waiver of all support-cost charges cannot be justified. Examples of the systematic waiver of such charges include the United Nations Secretariat's humanitarian emergency trust funds, UNESCO trust funds, and "counterpart contributions" to UNEP. All extrabudgetary contributions incur support costs and should provide for the recovery of at least some of these costs.

IV. TOWARDS HARMONIZATION OF POLICY PRINCIPLES

A. Competition

53. As a result of stagnating or declining core resources, United Nations system organizations have no choice but to compete for extrabudgetary resources if they are to avoid a rapid decline in their normative and operational expertise, and ultimately, their global relevance. A significant number of United Nations system organizations are facing financial management challenges as a result of having to compete for resources; smaller United Nations system organizations may be particularly handicapped in this regard since they are less likely to benefit from administrative economies of scale. Notwithstanding the fact that donors should focus on total support costs, direct and indirect, as well as on the specialised expertise of individual United Nations system organizations, evidence suggests that "competitive" support-cost rates are factors in the mobilization of extrabudgetary resources. These "competitive" rates, however, may lead to further declines in support-cost income. The pressure to compete for extrabudgetary resources may also lead to the implementation of policies that conceal indirect support costs within substantive project inputs and expenditures (see paragraphs 41 and 42).

54. It is difficult to determine the extent of competition for extrabudgetary resources between United Nations system organizations; particularly as far as it is influenced by support-cost rates. The responses of the questionnaire suggest that competition between specialized agencies is relatively limited; these organizations apply more or less the same support-cost policies. Competition between the specialized agencies and the funds and programmes is almost certainly more significant: the most frequently cited organization in this respect is UNOPS.

55. For competition between United Nations system organizations to exist, these organizations must be operating in the same "markets": hence the lack of competition between the specialized agencies. In this regard, where programme activities are the preserve of a single United Nations system organization, particularly one without obvious non-United Nations competitors, donors are unlikely to be as influenced by support-cost rates as they are where a number of organizations are competing to perform the same activity. Similar or overlapping mandates and common programme activities are the likely cause of this competition. The complex interrelationships between education, health and children as components of "development", for example, or refugees, food, medicines and children as components of a "humanitarian" crisis, present difficulties for the elimination of overlapping mandates/activities and the corresponding competition between United Nations system organizations for extrabudgetary resources. However, since the majority of United Nations system organizations operate in an environment populated by an ever-expanding number of non-United Nations entities, further competition for extrabudgetary resources is unavoidable.

56. There is no evidence to suggest that low support-cost rates applied by United Nations system organizations are based upon demonstrable comparative efficiency; such a determination would require a system-wide cost-measurement exercise. Nevertheless, where Member States approve comparatively high–or comparatively low–support-cost rates, they undoubtedly create a situation where some organizations have a comparative advantage over others in the mobilization of extrabudgetary resources for common activities. The significance of this comparative advantage, or disadvantage, should not be underestimated as donors may regard organizations with low support-cost rates as more efficient.

B. Harmonization

57. Past harmonization of support-cost rates was the direct result of the once-dominant role played by UNDP in technical cooperation (see paragraphs 11-13 and 27). The United Nations system has changed considerably since the 1970s, however, and the previously clear distinctions between funding and executing entities have either blurred or become irrelevant. At best, support-cost rates are highly aggregated estimates based upon an individual organization's cost-recovery requirements. A diverse range of support-cost rates reflects a diverse range of cost structures and the different priorities attached by legislative bodies to the support and implementation of specific categories of extrabudgetary activity. In

this regard, the costs associated with the establishment and application of a single, system-wide support-cost rate would almost certainly outweigh the benefits. The United Nations system lacks the necessary system-wide functional, financial, substantive and political homogeneity upon which to base a system-wide support-cost rate, or even a simple schedule of rates.

58. Almost all United Nations system organizations surveyed favour a measure of support-cost harmonization but at a conceptual level rather than at the level of support-cost rates. Many respondents consider that the harmonization of support-cost rates is not feasible on the grounds that United Nations system organizations do not have the same cost structures. Staff costs constitute the most important element in almost all United Nations cost structures and are therefore the most obvious example of significant differences between these structures. Staff salaries include an important post adjustment component, ensuring that no matter where United Nations common system staff work, take-home pay by grade has a purchasing power equivalent to that at the base of the system, New York. Staff salaries may also include components for hardship or hazardous conditions. A system-wide support-cost rate cannot accommodate variations in staff costs and would inevitably result in wide variations in the degree to which such costs are recovered. A system-wide support-cost rate would have precisely the opposite effect on support-cost recovery, would weaken the United Nations system's competitive position vis-à-vis non-United Nations entities, and would reduce essential operational flexibility.

59. The extent to which a United Nations system organization recovers support costs, and by corollary, the degree to which its core resources support activities financed from extrabudgetary resources is a matter for decision by its legislative organ. As referred to in paragraph 12, this principle was highlighted by the ACABQ and endorsed by the General Assembly in resolution 35/217 of 17 December 1980.[27]

60. Nonetheless, a multiplicity of extrabudgetary support-cost rates does not preclude harmonization of the principles upon which such rates are based. For instance, a number of respondents indicated that a degree of harmonization of support-cost policies is also an important aspect of the collaborative relationships required, for instance, by joint programming. The development of a common approach to the establishment of these rates will, inter alia, improve Member States' understanding and acceptance of support-cost policies of United Nations system organizations. A transparent and consistent approach to the establishment and application of support-cost rates will greatly enhance their legitimacy and facilitate the recovery of extrabudgetary support costs.

61. Support-cost policies must ensure that extrabudgetary resources continue to be mobilized and deployed effectively to further mandated activities in developmental, humanitarian and other substantive areas. They should be straightforward, transparent, easy to administer, and provide for a more consistent approach to special arrangements (to ensure the equal treatment of Member States and other donors). To this end, extrabudgetary support-cost rates should be established in accordance with the following principles:

> They should recognize and reflect the relative centrality and direct benefits of an extrabudgetary activity to the mandated programme, i.e., support-cost rates applied to extrabudgetary resources for activities that correspond with the programme priorities established by an organization's legislative body should be lower than those for more marginal activities;
>
> They should be differentiated by type of activity, conditionality and the volume of resources, i.e., recognition should be accorded to the fact that administrative costs: vary in accordance with the complexity of the activity being financed; vary in accordance with the complexity of special administrative, oversight and reporting conditions required by donors; and, benefit from economies of scale.

62. When establishing new extrabudgetary support-cost rates, careful prior consideration must be given to the effect of these changes upon administrative income, ensuring at the same time that a larger proportion of the costs associated with supporting extrabudgetary activities does not fall upon core

[27] A/35/544, op. cit.

resources. In this respect, any reduction in support-cost rates must be justified on the grounds that such reductions will not negatively impact upon the recovery of extrabudgetary support costs: by implementing administrative reforms and other policies that promote more efficient support of extrabudgetary activities and/or by demonstrating that lower support-cost rates will increase extrabudgetary income and generate economies of scale. Respondents to the questionnaire highlighted the importance of administrative efficiencies in reducing extrabudgetary support costs. The most significant measures in this respect include: the streamlining of administrative procedures and processes; the standardization and broader application of information technology; the establishment of common services; the decentralization of administrative and project management functions; outsourcing; and the replacement of international staff with national professional officers.

63. The executive heads of United Nations system organizations are already authorized to accept extrabudgetary contributions subject to certain conditions (see paragraph 17) and should perhaps be granted the authority to establish extrabudgetary support-cost rates based upon the principles described above (pending approval of those principles by legislative organs). The authority of executive heads to accept extrabudgetary contributions recognizes the uncertain and unpredictable nature of these resources and the impracticalities associated with their acceptance by legislative organs. It also recognizes the fact that executive heads are in the best position to determine what extrabudgetary activities can be accommodated within a core programmes implementation schedule. Since the costs associated with supporting extrabudgetary activities are dependent to a large degree upon the nature of the activities to be supported, the rate(s) to be applied to the recovery of these costs needs to be tailored accordingly. The executive heads of United Nations system organizations are best placed to take practical and timely decisions as regards the most appropriate support-cost rates to be applied to specific extrabudgetary activities. Just as the executive heads of United Nations system organizations are authorized to accept extrabudgetary contributions within certain policy and reporting parameters, they could be authorized to establish support-cost rates, provided that they do so in accordance with the principles described in paragraph 61 and report thereon to legislative organs.

64. The process of establishing and applying support-cost policies should be monitored by the United Nations System Chief Executives Board for Coordination (CEB), and regular comparative reporting of such policies should be developed and disseminated. The outcome of this reporting should be reviewed by the appropriate CEB machinery, with a view to harmonizing, to the extent possible, the principles underlying support-cost policies, and by executive heads, who would report thereon to their respective legislative organs.

65. The delegation of authority to executive heads of United Nations system organizations to establish extrabudgetary support-cost rates in no way constitutes an abrogation of the responsibilities of legislative organs to oversee the financial management of United Nations system organizations. Legislative organs should continue to monitor overall administrative and other support expenditures and to review these components in the budgets of United Nations system organizations. In doing so, Member States should ensure that administrative and other support requirements in core budgets do not increase in proportion to overall core resources and that increases in extrabudgetary resources do not generate increased administrative and other support requirements from core resources.

Annex

Reservations or dissenting views expressed by the organizations with regard to the recommendations and related findings

Introduction

1. This annex is the first to be prepared by JIU in response to the United Nations General Assembly request to the Unit, in para. 7 of its resolution 56/245 of 24 December 2001, "to consider including in its reports, where possible, the comments of the participating organizations on its findings and recommendations…".

2. Seeking the comments and observations of participating organizations on draft JIU reports is a systematic step in the process of preparation of the reports. Every effort is made by the Inspectors to take into account and incorporate, as appropriate, in the final version of the reports, the comments and observations received on each of the recommendations as well as on specific paragraphs contained in the draft. This, however, may not always be possible due to difficulties in reconciling divergent views, in some cases among the organizations themselves (when the report is system-wide or involves more than one organization), in other cases between the Unit on one hand and the organization(s) on the other.

3. In order to meet the request of the General Assembly in a concise manner and to highlight for the benefit of Member States any persisting differences of views, the Unit requested participating organizations to provide it with any reservations or dissenting views they might still have on the final version of the report. This annex presents basically those reservations or dissenting views, as expressed by the organizations, on the recommendations and related findings of the report.[1]

4. As a system-wide report, comments were sought from all JIU participating organizations. Responses to and comments on the final version of the report were received from the following organizations: the United Nations, including most of its programmes, funds and offices (UNICEF, UNCTAD, UNDP, UNEP, UNFPA, UNDCP, WFP, and UNHCR); ILO; FAO; UNESCO; ICAO; WHO; UPU; ITU; WMO; IMO; WIPO; UNIDO; and IAEA.

5. The reservations or dissenting views are presented in two parts: the first part reflects general comments from the organizations on the overall thrust of the report, while the second deals with comments related to specific findings and recommendations.

I. General comments

The report and its general thrust towards harmonization of policy principles related to support costs in the UN system organizations was well received and welcomed by the secretariats of participating organizations. ICAO, however, expressed the following views: "ICAO does not contribute to the view that there should be a common UN system cost-recovery policy. Given the variance in the nature and purpose of extrabudgetary contributions as well as the technical cooperation programmes, each organization should be able to establish policies that are acceptable to its governing organs and its clients".

II. Specific comments on findings and recommendations

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[1] It should be noted that, this being the first time JIU has followed this procedure, some organizations simply repeated or referred to their previous comments on the draft report. Such comments, which, in the view of the Inspectors, did not represent or amount to reservations or dissenting views are not included in this annex.

Recommendation 1

United Nations

"Recommendation 1 is less relevant to the UN than it is to other Organizations in the UN system. Since 1974-75, Proposed Programme Budget presentations have integrated extrabudgetary resources with regular budget resources. Over successive biennia, the degree of detail and other aspects of the presentation of extrabudgetary resources in proposed programme budgets have been amended in accordance with recommendations of the Advisory Committee on Administrative and Budgetary Questions. In view of the present degree of integration; the Advisory Committee's role as regards programme and peacekeeping budgets; the extremely long and difficult review and approval process for assessed budgets; and the fact that extrabudgetary resources not already subject to intergovernmental review and approval (i.e. excluding UNHCR, UNRWA and UNEP) are still a relatively low proportion of total resources, [UN] would prefer that these resources are not subject to intergovernmental approval. Until such time as the UN's budget review and approval process is streamlined, or 'unapproved' extrabudgetary resources become an even more significant share of total resources, the existing policy should continue to apply."

FAO

"FAO fully accepts that extrabudgetary resources should only be accepted consistent with the policies, aims and activities of the Organization – that is, they must be in accord with the programmatic priorities approved by the legislative bodies...[However], FAO is of the view that this is a much more complex issue than can be handled in the context of a report on support costs. For example, we [FAO] are concerned that it does not recognize the significant difference between extrabudgetary resources in support of the Regular Programme versus those in support of technical cooperation assistance at country level. Nor does it define whether the extent of extrabudgetary resources to be incorporated in budget presentations is dealing with a descriptive view (i.e. a forecast of likely receipts) or of the prescriptive requirements (i.e. the hoped-for level of receipts). In conclusion, it is FAO's view that the issue might best be raised in another context (which would imply deleting recommendation 1 from this report)."

ILO

"The report raises other issues that are much larger [than its intended focus on support costs related to extrabudgetary activities] and would widen the debate once the report is brought before any legislative body. One such issue is related to the integration of extrabudgetary resources with core resources in budget presentations and the programmatic prioritization of extrabudgetary resources (in particular paragraph 8 of the report). Although this is a complex issue, it is dealt with rather summarily in the report and is then part of the recommendations. The subject should either be addressed in a more comprehensive manner or it should be deleted, at least as far as the recommendations are concerned; otherwise it would lead to confusion in subsequent discussions in legislative bodies...The JIU does not seem to acknowledge in the report that extrabudgetary contributions are made by donors in areas that interest them. There is very limited scope for the Office to determine what can be done with said contributions. This being said, the ILO has been successful with some discretion by the Director-General." [2]

[2] In its comments on this recommendation, ILO also mentioned that "[it] does provide an indication of extrabudgetary activities in its presentations of its regular core budget. Moreover, in the discussions of the Governing Body Committee on Technical Cooperation, the ILO informs the Governing Body on a systematic basis on its resources, expenditures and activities related to extrabudgetary activities. The Office has also indicated in its proposals what could be done should additional extrabudgetary resources be made available."

UNESCO

"We [UNESCO] have difficulty in agreeing to the recommendation to have extrabudgetary amounts subject to legislative approval, given that the General Conference, up until now, only approves regular budget resources on the basis of which Member States contributions are assessed. We have always taken the position that extrabudgetary funds are indicative and there is no certainty that the funds pledged would be received, hence serious difficulty in planning."[3]

Recommendation 3

FAO

"FAO accepts recommendation 3 but not the premise that it is implied by the preceding text (i.e. in the Executive Summary)…Our [FAO] view is that this text…seems to deny the value of standard cost accounting practices as an appropriate approach to developing sound management information on which to base decisions. FAO's view is that it is proper, as is recommended, to require that the costs and benefits of any approach to cost measurement be taken into account but that it is not correct to conclude on the limited evidence available that a given methodology is not appropriate or cost beneficial."[4]

Recommendation 4

ICAO

"With respect to interest received on funds deposited for extrabudgetary activities, ICAO is of the view that such interest should be returned to donors, as full support costs are already being recovered from the donors. Donors could then decide how they wish to use the interest income. ICAO's position is based on the following: (a) interest income, given its precarious nature, cannot be relied upon as a source of income to meet the expenditures of [its] Technical Cooperation Bureau, which is required to operate on a self financing basis; (b) the refund of interest is coherent with ICAO's requirement for project funds to be deposited in advance before implementaion…; (c) since the support cost charges for [its] Technical Cooperation Programme projects already takes into account the entire estimated cost of implementing the projects, retention of interest would be inherently inequitable."

ILO

"It is not for the legislative organs to determine what can or cannot be done with interest earned on extrabudgetary funds. Extrabudgetary funds are donor funds. Any interest earned on such 'funds in trust' belongs to the donor unless the donor specifically agrees otherwise. It is possible that some organizations'

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[3] UNESCO most recently opted "to indicate at the main line of action level a global figure for regular budget and extrabudgetary resources, the latter being the figure for "existing projects" for which funds have actually been received for implementation in the new biennium…this global figure should then be followed by individual figures for regular budget and extrabudgetary resources."

[4] It is worth noting in this context that, for example, WHO expressed the following view on this same finding and recommendation: "WHO agrees with this recommendation. Quite rightly, the JIU expresses skepticism about the management accounting value of such "*cumbersome, costly and time-consuming time-work surveys*". These generally use an incremental approach to the determination of support costs, while the JIU points out that the process of defining incremental costs entails an unavoidable element of subjective judgment. WHO undertook such an exercise prior to considerations by the Executive Board in 1996 of a higher PSC rate. Studies have been conducted showing that the "true" support cost borne by WHO when providing the full range of the administrative services to a given extarbudgetary programme or entity were generally sizeably higher than the present approved rate of 13%. The Executive Board did not, however, approve a higher rate."

financial regulations may not provide for this, but this is not the case in the ILO."

UNEP

" We [UNEP] agree with all the recommendations except for recommendation 4...Some donors insist that any interest income generated by their extarbudgetary contributions belongs to the donor and has to be paid back to them, others are willing to allow the concerned agency to retain the interest provided that the donor has a say on their utilization...in the case of UNEP, quite often the interest is used to support the activities to cover for shortfalls in the required resources."

UNDP

"It is not the Executive Board that controls the handling of interests. It is the agreement with the donors that decides whether interest is retained or refunded."

Recommendation 6

ILO

"This recommendation assumes dissatisfaction [from donors] with the 13% charge, which the ILO has only encountered to a limited extent. Most of the multi-bilateral donors, at present have not raised this at all."

WHO

"This is an extremely interesting suggestion from JIU for achieving more programme support cost (PSC) flexibility and enabling organizations such as WHO to compete on a more equal footing with those others who already employ this practice. However, there are also drawbacks in shifting some cost elements over from the "lump-sum category" covered by a standard PSC rate to itemized direct cost elements individually reimbursable as such: firstly, any such shift may lead to suggestions for a corresponding reduction in the list of permissible PSC cost elements, which in turn could lead to demands for an overall lowering of the standard PSC rate; secondly, the report itself implicitly admits, and as is indicated in recommendation 1, that extrabudgetary resources are being (and should be) increasingly mainstreamed into the integrated programmatic action of an organization. Recourse to direct costs, by contrast, may end up promoting project-specific grants, programme fragmentation and micro-management. This is especially true of Foundation-type support."

Recommendation 9

WHO

"We [WHO] agree that it is the core duty of any administration to continually strive for maximum efficiency of administrative services, but feel that any gains thus realized should not be considered to be the exclusive "property" of the extrabudgetary part of the Organization's activities."